

BEFORE THE UTAH STATE TAX COMMISSION

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PETITIONER 1 & PETITIONER 2,

Petitioners,

v.

AUDITING DIVISION OF THE UTAH STATE  
TAX COMMISSION,

Respondent.

**ORDER**

Appeal No. 06-1592

Account No. #####

Tax Type: Income Tax

Tax Years: 1999, 2001

Judge: Phan

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**Presiding:**

Jane Phan, Administrative Law Judge

**Appearances:**

For Petitioner: PETITIONER 1

For Respondent: RESPONDENT REPRESENTATIVE 1, Assistant Attorney General  
RESPONDENT REPRESENTATIVE 2, Tax Audit Manager  
RESPONDENT REPRESENTATIVE 3, Senior Auditor

STATEMENT OF THE CASE

This matter came before the Commission for an Initial Hearing on May 21, 2007. At the hearing Petitioner contested an audit deficiency of additional income tax and the interest accrued thereon for tax years 1999 and 2001. The Statutory Notices of Audit deficiency were issued on October 31, 2006 for tax year 1999 and November 8, 2006 for tax year 2001. No penalties were assessed. The amount at issue for each year is as follows:

Year	Tax	Interest <sup>1</sup>	Total
1999	\$\$\$\$\$	\$\$\$\$\$	\$\$\$\$\$
2001	\$\$\$\$\$	\$\$\$\$\$	\$\$\$\$\$

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<sup>1</sup> Interest continues to accrue on the unpaid balance.

APPLICABLE LAW

Utah imposes income tax on individuals who are residents of the state, in Utah Code Sec. 59-10-104 as follows:

...a tax is imposed on the state taxable income, as defined in Section 59-10-112, of every resident individual...

State taxable income is defined in Utah Code Sec. 59-10-112 as follows:

"State taxable income" in the case of a resident individual means his federal taxable income (as defined by Section 59-10-111) with the modifications, subtractions, and adjustments provided in Section 59-10-114 . . .

Federal taxable income is defined in Utah Code Sec. 59-10-111 as follows:

"Federal taxable income" means taxable income as currently defined in Section 63, Internal Revenue Code of 1986.

A deduction from taxable income for health insurance premiums is provided is provided at Utah Code Sec. 59-10-114(2) (2001)<sup>2</sup> as follows:

There shall be subtracted from federal taxable income of a resident or nonresident individual: . . . (h) Subject to the limitations of Subsection (3)(e), amounts a taxpayer pays during the taxable year for health care insurance, as defined in Title 31A, Chapter 1, General Provisions: (i) for: (A) the taxpayer; (B) the taxpayer's spouse; and (C) the taxpayer's dependents; and (ii) to the extent the taxpayer does not deduct the amounts under Section 125, 162, or 213, Internal revenue Code, in determining federal taxable income to the taxable year; . . .

However the health insurance premium deduction is further limited by provisions set out at Utah Code Sec. 59-10-114(3)(e) (2001), which states:

For purposes of Subsection (2)(g), a subtraction for an amount paid for health care insurance as defined in Title 31A, Chapter 1, General Provisions, is not allowed: (i) for an amount that is reimbursed or funded in whole or in part by the federal government, the state, or an agency or instrumentality of the federal government or the state; and (ii) for a taxpayer who is eligible to

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<sup>2</sup> The Commission applies the law in effect during the period in question. The current versions of these code sections have been renumbered and have had revisions.

participate in a health plan maintained and funded in whole or in part by the taxpayer's employer or the taxpayer's spouse's employer.

A credit is allowed for taxes paid to another state at Utah Code Sec. 59-10-106 (1) (1999) which provides:

A resident individual shall be allowed a credit against the tax otherwise due under this chapter equal to the amount of the tax imposed on him for the taxable year by another state of the United States, the District of Columbia, or a possession of the United States, on income derived from sources therein which is also subject to tax under this chapter.

#### DISCUSSION

There were two different issues in this matter. For tax year 2001 the issue was Respondent's denial of the health insurance premium deduction under Utah Code Sec. 59-10-114(2) & (3). For the tax year 1999 the issue was a disallowance of a credit for taxes paid to another state under Utah Code Sec. 59-10-106.

Considering the first issue, Petitioner and his family did not have traditional health insurance during 2001. Petitioners represented that neither of them were eligible to participate in a health plan maintained or funded by an employer. Instead they participated in a health care cost sharing organization or cooperative, which was the ORGANIZATION. They paid monthly amounts to participate in this organization and deducted on their 2001 Utah individual income tax return an amount of \$\$\$\$ as a health care premium deduction.

Petitioners' position was that this was similar to health care insurance premiums, although they acknowledged the ORGANIZATION was not an insurance company. Petitioners paid a monthly contribution, if they needed medical care they would go to the doctor or hospital as necessary and Petitioners were responsible for the medical bills, which they would pay. Then they could submit a claim to the cooperative and they would expect to eventually be reimbursed when there were funds available. The website ( X ) described the cooperative as follows:

ORGANIZATION is not an insurance company. As a voluntary cost-sharing program we do not assume responsibility or the legal obligation for your medical bills. Members share your qualifying medical bills through their monthly gift amounts. In the past 15 years, ORGANIZATION members have shared more than \$\$\$\$ million in medical costs!

Although this cooperative provides some of the benefits of a medical insurance plan, it is not health care insurance as defined in Title 31A, Chapter 1, General Provisions. There is no “transfer of risk” or “assumption of risk” as required by those provisions. Petitioners may not deduct as medical insurance premiums the amounts they paid toward this medical cooperative from their taxable income for the purposes of determining their Utah Individual Income Tax. Respondent appropriately disallowed this deduction.

The second issue was a credit in the amount of \$\$\$\$ that Petitioners claimed on their 1999 Utah return for taxes paid to another state. On Schedule A of their Utah return, they indicated that they had paid \$\$\$\$ in taxes to STATE for the 1999 tax year. When determining the amount of the credit for their Utah return on Schedule A this amount was subject to the credit limitations, which reduced the amount of the credit claimed to \$\$. At the time the Statutory Notice of Audit Change was issued, Respondent had denied this credit in its entirety. At the hearing, Respondent indicated that based on the STATE return that Petitioners submitted after the audit was issued, Respondent would accept a credit in the amount of \$\$\$\$, which was the total STATE tax that Petitioners claimed on their Nonresident STATE Income Tax Return for that year. Petitioners had not prepared the STATE return until 2006.

It was Petitioners’ position that despite their actual tax liability as claimed on their late-filed STATE income tax return, they actually had paid taxes to STATE during 1999 totaling \$\$. A portion of this amount, \$\$, was paid in 1999 but was for a tax issue arising in 1997. Petitioners explained that STATE had placed a lien on property Petitioners owned in that state for an inputted tax liability from 1997. When Petitioners sold the property in 1999, STATE exercised the lien and collected \$ of the proceeds. Also on that sale of the property, STATE automatically withheld \$ of the proceeds anticipating

Petitioners' gain from the sale would result in an income tax liability to that state. Petitioners were Utah residents and were not familiar with the STATE law. They did not understand that they could have received most of this money back by filing the proper return, so they did not do so. When they learned years later that they would have been entitled to a refund of most of this withholding, it was too late for them to obtain the refund. So STATE had kept the withholding despite that when Petitioners prepared a 1999 STATE Nonresident Return late in 2006, they calculated a total income tax liability for STATE of only \$\$\$\$\$.

Tax credits are strictly construed,<sup>3</sup> therefore, the circumstances must fit directly within the statutory provisions. Utah Code Sec. 59-10-106 (1) provides the credit is allowed "equal to the amount of tax imposed on him for the taxable year by another state . . . on income derived from sources therein which is also subject to tax under this chapter. The tax lien related to 1997 was not tax imposed on Petitioner for tax year 1999, it related to 1997 and therefore, does not qualify for the credit for that reason. Additionally, it may not qualify for the credit for the same reason as the withholding paid at the time of the sale to the state of STATE, because it was not tax imposed on Petitioners for the taxable year by STATE. When Petitioners finally prepared the STATE return they calculated their STATE tax to be only \$\$\$\$\$.

#### DECISION AND ORDER

Based upon the foregoing, the Commission sustains the audit deficiency of additional income tax and interest against Petitioners for tax year 2001. Respondent is to adjust its audit for tax year 1999 to allow credit for taxes paid to STATE in the amount of \$\$\$\$\$. It is so ordered.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall

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<sup>3</sup> See *Union Pacific R.R. v. Auditing Div.*, 842 P.2d 876, 880 (Utah 1992); *Parsons Asphalt Prods., Inc. v. State Tax Comm'n*, 617 P.2d 397, 398 (Utah 1980); *SF Phosphates LTD v. Auditing Div.*, 346 Utah Adv. Rep. 18 (Utah 1998); and *MacFarlane v. Utah State Tax Comm'n*, 2006 UT 25 (2006).

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be mailed to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission  
Appeals Division  
210 North 1950 West  
Salt Lake City, Utah 84134

Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this \_\_\_\_\_ day of \_\_\_\_\_, 2007.

\_\_\_\_\_  
Jane Phan, Administrative Law Judge

BY ORDER OF THE UTAH STATE TAX COMMISSION:

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this \_\_\_\_\_ day of \_\_\_\_\_, 2007.

Pam Hendrickson  
Commission Chair

R. Bruce Johnson  
Commissioner

Marc B. Johnson  
Commissioner

D'Arcy Dixon Pignanelli  
Commissioner

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